MINUTES
of the
SIXTH MEETING
of the
INVESTMENTS AND PENSIONS OVERSIGHT COMMITTEE

November 7, 2013
Room 322, State Capitol
Santa Fe

The sixth meeting of the Investments and Pensions Oversight Committee (IPOC) for the 2013 interim was called to order by Representative Jim R. Trujillo, chair, on Thursday, November 7, 2013, at 9:18 a.m. in Room 322 of the State Capitol in Santa Fe.

Present
Rep. Jim R. Trujillo, Chair
Sen. Sue Wilson Beffort
Sen. Jacob R. Candelaria
Sen. Carroll H. Leavell
Sen. Steven P. Neville
Sen. Bill B. O'Neill
Rep. Jane E. Powdrell-Culbert
Rep. William "Bill" R. Rehm
Rep. Luciano "Lucky" Varela

Absent
Sen. George K. Munoz, Vice Chair
Rep. Larry A. Larrañaga
Rep. Henry Kiki Saavedra
Sen. William P. Soules

Advisory Members
Rep. Donald E. Bratton
Sen. Carlos R. Cisneros
Rep. Miguel P. Garcia
Rep. Roberto "Bobby" J. Gonzales
Sen. Stuart Ingle
Sen. Timothy M. Keller
Sen. Mary Kay Papen
Rep. William "Bill" J. Gray
Rep. Emily Kane
Rep. Tim D. Lewis
Rep. Patricia A. Lundstrom
Sen. William H. Payne
Sen. John C. Ryan
Sen. Michael S. Sanchez
Rep. Sheryl Williams Stapleton

Staff
Claudia Armijo, Staff Attorney, Legislative Council Service (LCS)
Amy Chavez-Romero, Assistant Director for Drafting Services, LCS
Pam Stokes, Staff Attorney, LCS
Ric Gaudet, LCS

Guests
The guest list is in the meeting file.

Handouts

Handouts and other written testimony are in the meeting file.

<u>Thursday, November 7</u>

Recent Investment Performance of and Legislation Proposed by the State Investment Council (SIC)

Steven K. Moise, state investment officer, and Vince Smith, deputy state investment officer, SIC, discussed with the committee the investment performance of the SIC and proposed legislation. As of September 30, the SIC had $17.84 billion in assets under management. The current calendar year investment returns show a 10.5 percent return, outpacing the 7.5 percent annual target. The SIC has realized $1.7 billion in investment gains in 2013. Investment returns have been improving against policy indexes and benchmarks over time. However, the Severance Tax Permanent Fund (STPF) continues to lag behind market returns because that fund is required to invest a portion of its assets in New Mexico-based economically targeted investments (ETIs).

In 2011, the SIC studied its investment allocation strategy and subsequently adopted new allocation strategies designed to diversify its investment portfolio and to create more income. The SIC has been systematically decreasing its public equity exposure to decrease volatility, and it has been increasing investment in income-producing portfolios, including real assets, real estate and credit-based investments.

The SIC is seeking an amendment to the Constitution of New Mexico to allow more flexible investment standards for the Land Grant Permanent Fund (LGPF). The proposed amendment would eliminate the 15 percent maximum of investment of the fund in international securities and increase the standard of care for investment of the fund. The SIC is also currently looking at legislation to stabilize deposits into the STPF, which has not had significant deposits into the fund for many years. The state needs to gradually increase the amount deposited into the fund in order for it to remain a truly useful trust fund.

Questions and comments from committee members included the following.

- What would be the consequence of removing the 15 percent investment cap on international securities from the LGPF legislation? Charles Wollman, spokesperson, SIC, said that this change will not mean dramatic changes in the way the SIC invests the fund. The SIC would not be able to invest 75 percent of the fund in international securities, as was widely believed in the legislature during the past session.

- The SIC does not seem to like ETIs because their return is not as high as other investments. However, those investments have benefited the residents and economy of the state much more than could have been possible by just using the slightly larger distributions from the fund to invest in those activities.

The legislation proposed by the SIC, Draft #1 in the IPOC proposed legislation booklet, was endorsed unanimously by the committee.

Approval of Minutes

The minutes from the October 16, 2013 meeting of the committee were adopted without changes.

New Actuarial Valuations of the Educational Retirement Board (ERB)

Jan Goodwin, executive director, ERB, presented the actuarial valuation of the Educational Retirement Fund as of June 30, 2013 to the committee. The actuarial funded ratio declined from 60.7 percent to 60.1 percent from the previous year's valuation, and the unfunded actuarial accrued liability (UAAL) increased from $6.2 billion to $6.5 billion. These calculations are determined as of a single point in time and do not reflect recent legislation making dramatic changes to contribution levels and retirement benefits.

The actuarial valuation for 2013 reflects updates in the recently completed experience study, which made changes to assumptions about mortality, retirement and termination and decreased wage inflation and payroll growth. The valuation also reflects the total fiscal year 2009 asset loss during the recent recession. Future actuarial valuations should show gains in the funded ratio of the fund, said Ms. Goodwin.

Ms. Goodwin reported that for fiscal year 2013, the ERB will not be required to use a blended discount rate to determine its UAAL.

Questions and comments from committee members included the following.

- With the new accounting rules requiring blended discount rates for those portions of pension liability not contained in current assets, pension boards will be tempted to project higher return rates to minimize the blending requirement. Ms. Goodwin said that the ERB only uses the discount rate based on its own experience and based on actuary recommendations.

- Why is the ERB's UAAL projected to increase until 2028? Ms. Goodwin said that the increased employee and employer contribution rates will take some time to turn the fund's balance sheet around.

Proposed Legislation for Legislative Retirement Changes

Representative Garcia presented proposed legislation (Draft #5) for the committee's consideration that would eliminate legislative retirement for all new legislators beginning service on or after January 1, 2015 and would eliminate cost-of-living increases for retired legislators. Legislators and other public officials should serve the public and not themselves. Representative Garcia said that no public official should receive a pension, and this legislation would be a first step in that direction.

After discussion of the merits of the bill by committee members, Representative Garcia withdrew the legislation from the committee's consideration.

Legislation Proposed by the Retiree Health Care Authority (RHCA)

Mark Tyndall, executive director, RHCA, presented proposed legislation (Draft #2) for the committee's consideration that would incrementally increase employer and employee contributions into the Retiree Health Care Fund. The fund is expected to run a deficit beginning in 2021 and will be completely depleted by 2029 under the current situation. The RHCA implemented many reforms to the retiree health care program, including increasing premiums, reducing certain subsidies, increasing cost-sharing and increasing the years of service required to obtain the maximum subsidy received. The biggest change to the solvency of the fund is increasing contribution levels, which requires legislative action.

The legislation would increase over six years employee and employer contributions by 57 percent. Employee contributions would increase from one percent of salary to 1.75 percent of salary, and employer contributions would increase from two percent of salary to 3.5 percent. The revenue generated from these contribution increases will extend the solvency of the fund through 2043.

Questions and comments from committee members included the following.

- What was the impact on the solvency of the fund by the reductions in state employee payroll over the past few years? Mr. Tyndall said that the fund lost three years of solvency from the reductions in state employment.
- The RHCA should consider a minimum age of 62 for employees before receiving subsidized benefits.
- One big reason the fund solvency is an issue today is that the previous administration drastically lowered premiums, which quickly expended much of the balance in the fund.

The committee endorsed the RHCA legislation on a vote of 5-3. The RHCA will find a sponsor for the bill.

New Actuarial Valuations and Funding Projections of the Public Employees Retirement Association (PERA)

Wayne Propst, executive director, PERA, presented the committee with a summary of the PERA fund's actuarial status. The fund reached an all-time high of $13.8 billion in October, representing the recovery of all assets lost during the 2007-2009 market downturn. In fiscal year 2013, the fund had an investment gain of $1.2 billion, a 13 percent gain. Passage of recent legislation changing contribution levels and reducing the cost-of-living adjustment (COLA) had an immediate impact on the fund's UAAL, decreasing it from $6.2 billion to $4.6 billion. Before the legislation, the PERA fund was expected to be nearly insolvent by 2053, but it is now expected to be well above 100 percent solvency by that year.

Mr. Propst cautioned that the significant decrease in the PERA fund's UAAL was a one-time event. Future decreases will be more gradual. In addition, the PERA actuary will do a new experience study in 2014, which may change some of the assumptions made in determining funded ratios.

Questions and comments from committee members included the following.

- Employees got stuck with the biggest contribution increase of an additional 1.5 percent of salary, while employers will only pay .4 percent extra.

- Once the funded ratio of the PERA fund reaches 100 percent, it may be desirable to reduce employee contribution levels or to increase benefits.

Legislation Proposed by the Administrative Office of the Courts (AOC)

Chief Justice Petra Jimenez Maes, New Mexico Supreme Court, and Arthur W. Pepin, director, AOC, presented proposed legislation (Drafts #3 and #4) for the committee's consideration that would provide solvency for the judicial and magistrate retirement systems. Chief Justice Maes said that she had met with Governor Susana Martinez, and she hopes the governor will now support the legislation after vetoing similar legislation in 2013. Both bills made similar changes to various retirement provisions, including decreasing the service credit multiplier from 3.75 percent to 3.5 percent; increasing the maximum pension amount from 75 percent to 85 percent of final average salary (FAS); increasing employee contributions from nine percent to 10.5 percent of salary; increasing employer contributions to 15 percent of salary; using five years instead of one year to calculate the FAS; giving a two percent COLA only if the funded ratio of the fund (either the Judicial Retirement Fund or the Magistrate Retirement Fund, accordingly) exceeds 80 percent, but giving a two percent COLA every three years if the ratio threshold is not met; increasing the vesting threshold from five years to eight years; requiring employers to pay the employee contributions for nonparticipating judges and magistrates; and changing standard payment forms and survivor benefits to align better with regular PERA provisions. In order to make up for a serious shortfall in the Magistrate Retirement Fund, a one-time appropriation of $5 million would be made to that fund. The main difference between the current proposals and the bill vetoed by the governor is that the current proposals do not switch the funding of judicial pensions from docket fees to general fund revenue.

Questions and comments from committee members included the following.

- It seems strange to use court docket fees to pay for judicial pensions.

- Does the PERA support the proposed legislation? Mr. Propst said that the PERA board of directors will consider endorsing the legislation later in November. The board did not endorse or oppose the previous legislation, but felt that more work was needed.

- Requiring nonparticipating judges and magistrates to make contributions, only to refund those contributions after the jurist leaves office, seems like a strange way of trying to generate extra revenue.

Draft #3, which makes changes to the Judicial Retirement Act, was endorsed by the committee unanimously.

Draft #4, which makes changes to the Magistrate Retirement Act, was endorsed by the committee 6-1, with an appropriation added.

Legislation Proposed by Legislators for Consideration of Endorsement

Senator Candelaria presented proposed legislation (Draft #5) for the committee's consideration that would impose a minimum age of 55 for legislative retirement.

Draft #5 was endorsed by the committee with changes.

Senator Keller withdrew consideration of Draft #7, a memorial requesting a study of the feasibility of combining state investment functions.

Adjournment

There being no further business, the committee adjourned at 3:55 p.m.